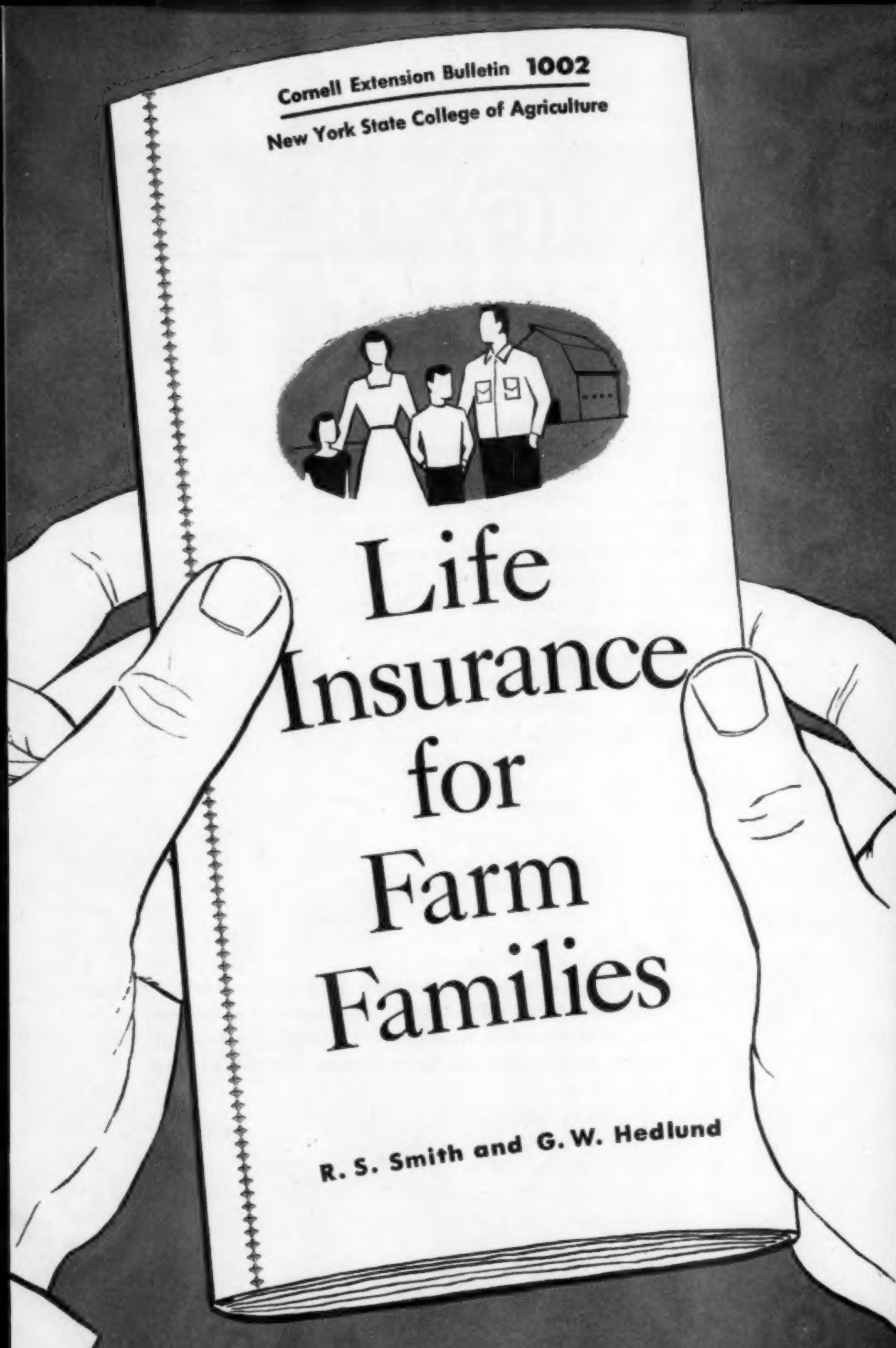
Cornell Extension Bulletin 1002
New York State College of Agriculture
Life
Insurance
for
Farm
Families
R. S. Smith and G. W. Hedlund

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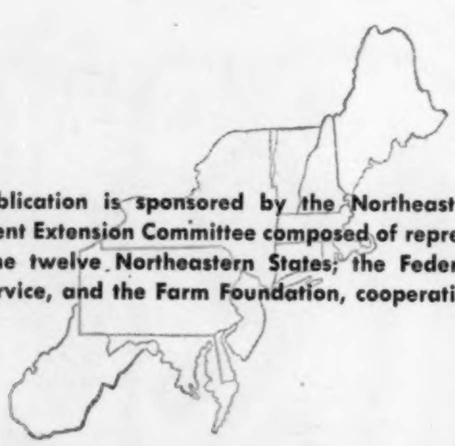

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Life Insurance for Farm Families

R. S. Smith and G. W. Hedlund

A sound life insurance program is of great importance to the financial security of a farm-owning family. It protects the family against the financial shock of the loss of the breadwinner. It can also be an important part of the family's plans for retirement, savings, use of credit, transfer of the farm to the next generation, and distribution of property at death.

Seventy per cent of all the people in the United States own life insurance of some kind.[1] At the end of 1956, there were 106 million owners of life insurance. The amount of life insurance carried totaled over $412 billion. The total, both in people and money, is still growing.

Acknowledgment: The authors wish to acknowledge the contribution of Dr. J. R. Tabb to this publication. Professor Tabb was formerly associated with the Department of Agricultural Economics at Cornell, and is at present Professor of Economics at College of William and Mary, Norfolk, Virginia.

[1]*Life Insurance Fact Book, 1957,* Institute of Life Insurance, New York.

Life insurance for the farmer is important not only for his family, but also for his business. A farm owner is a businessman. His life insurance needs are similar to those of other businessmen, but different from those of a salaried man. His life insurance program, therefore, should be considered as a part of farm planning as well as family financial planning.

The cost of life insurance is an important cash expense to farmers, taking its place with other forms of insurance, taxes and debt payments as necessary fixed cash outlays. Cash used to pay life insurance premiums means less cash to meet other family and farm expenses or to make profitable adjustments within the business itself. Because life insurance competes in this way for available cash, the farmer and his family must weigh the need for life insurance against other uses for those same dollars. A basic understanding of life insurance will help the family come to a sound decision.

Life insurance is big business and represents a broad field of study.

This bulletin does not attempt to cover the many aspects of this field. Its purpose is to help farm families understand the purpose of life insurance, the types of life insurance available, and the major needs for life insurance. The authors believe that many farmers do not spend their life insurance dollars wisely, and hope that this bulletin will help farmers build life insurance programs fitted to the needs of their families.

Life insurance should be purchased and maintained with an eye to overall financial planning. It is just one step in a farm family's financial plan. Other steps include keeping farm business insurance in line, using credit wisely, looking ahead to retirement, making the most of Social Security, considering a savings and investment program, and making a will and other plans for estate settlement. All these steps are interrelated and deserve consideration as one major problem in farm management and family finance.

Purpose of Life Insurance

The general principle underlying life insurance is that of spreading risk. Insurance spreads the risk by distributing the cost of one person's misfortune among a large number of persons. Most men hope to save up enough money before they die to pay their debts and to provide for dependent members of their family. However, many people die before they put in the expected number of working years. The death of the breadwinner at middle age places a heavy burden on those he leaves behind. An insurance policy will not prevent such a death. If the breadwinner is insured, however, the financial loss which comes to his family will be less severe.

Life insurance serves other purposes in addition to spreading risk. It is used as a means of systematic savings and as a form of investment.

How Life Insurance Works

Over 300 years of experience are behind modern life insurance. There is no guesswork about it. That any one individual may die this year or next is just a gamble, but the average number of deaths which will occur each year out of a group of 100,000 people of a given age can be predicted accurately. For many years information has been accumulated on death rates. On the basis of this information, insurance companies scientifically calculate the amount of insurance they can provide for a given number of dollars paid in premiums. Policyholders as a group pay for what they get; there is no magic in life insurance.

The commissioners 1941 Standard Ordinary Mortality Table is one which has been widely used in insurance. It is based on experience of life insurance companies under ordinary policies for the years 1930–1940.

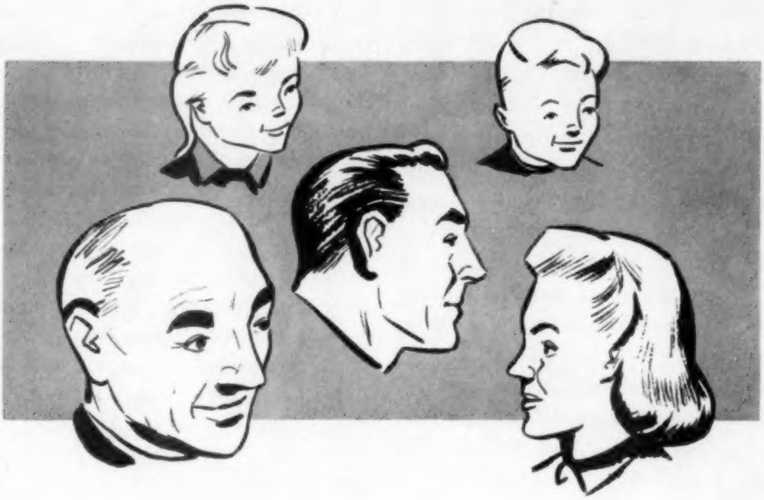


TABLE 1. COMMISSIONERS 1941 STANDARD ORDINARY TABLE OF MORTALITY

Age	Number living	Deaths each year	Deaths per 1,000	Expectation of life
1	1,000,000	5,770	5.77	62.76
5	983,817	2,715	2.76	59.76
10	971,804	1,914	1.97	55.47
15	962,270	2,069	2.15	50.99
20	951,483	2,312	2.43	46.54
25	939,197	2,705	2.88	42.12
30	924,609	3,292	3.56	37.74
35	906,554	4,161	4.59	33.44
40	883,342	5,459	6.18	29.25
45	852,554	7,340	8.61	25.21
50	810,900	9,990	12.32	21.37
55	754,191	13,560	17.98	17.78
60	677,771	18,022	26.59	14.50
65	577,882	22,907	39.64	11.55
70	454,548	26,955	59.30	8.99
75	315,982	28,009	88.64	6.82
80	181,765	23,966	131.85	5.06
85	78,221	15,185	194.13	3.66
90	21,577	6,063	280.99	2.58
95	3,011	1,193	396.21	1.63
99	125	125	1,000.00	.50

Source: Little Gem Life Chart, 1956, National Underwriter Company.

One big factor in life insurance, as opposed to fire and other types of insurance, is that death is certain. Only the time of death is in doubt. When life insurance is sold on an *annual* or term basis, the cost increases as the insured person gets older because his chances of death are greater. Most life insurance is sold on the *level premium* plan, and premiums remain the same as long as the policy remains in force.

There were over 1,100 legal reserve life insurance companies in operation in the United States in 1957. A breakdown of the income and expenses of these companies as reported by the Institute of Life Insurance provides an insight into the operations of the life insurance business. It shows that the major source of income in 1956 was premiums paid by policyholders. Because these premiums are not all paid out immediately as benefits, they must be invested and managed to produce income. This investment income made up about 20 per cent of total income. Less than half of the 1956 income was paid out in that year as benefits. Almost one-third was set aside as reserves against future claims to be paid.

TABLE 2. 1956 LIFE INSURANCE DOLLAR
U. S. Life Insurance Companies

Income:	
Premiums	80.2c
Net investment earnings and other income (before Federal taxes)	19.8c
	100.0c
How used:	
Benefit payments and additions to funds for policyholders and beneficiaries:	
Benefit payments in year	47.0c
Additions to policy reserve funds	27.9c
Additions to special reserve and surplus	3.9c
	78.8c
Operating expenses:	
Commissions to agents	7.8c
Home office and other expenses	9.4c
	17.2c
Taxes	3.2c
Dividends to stockholders	.8c
	100.0c

Source: Life Insurance Fact Book, 1957, Institute of Life Insurance.

Types of Life Insurance Policies

There are two main reasons why people buy life insurance:

1. As protection against loss of income in case of premature death.
2. As an investment or savings which will be used at some later date.

Stated another way, life insurance provides protection against two possibilities: (1) that the insured will die prematurely and leave dependents without income, (2) that the insured will live so long that he will be without income and thus become a burden on someone else.

Most people who buy life insurance want a combination of these two features of protection and investment. Some want only protection, while some want mostly investment. Insurance companies have combined the two features in a multitude of ways in order to be able to offer policies which will meet the needs of many different people. If a person wants to buy protection only, he can buy it at a lower rate than if it is combined with investment. The higher the investment feature of a policy, the higher the premium.

Every large insurance company offers a large number of policies. Basically, though, all policies can be classified as one of four main types. Here is how they work.

Term Insurance provides only protection and carries no investment feature. It is much the same as fire insurance. More protection can be purchased with $100 a year in term insurance than in any other kind. The protection is for a limited time only—usually for a five, ten, or fifteen year term. When the term is ended, the insurance has *no* cash value. At the end of the term, the policy must be renewed at a higher premium rate if the protection is to continue.

Straight Life or Ordinary Life Insurance is a plan of insurance for the whole of life with the premiums payable until death. Unlike term insurance, straight life is "permanent" in nature. The contract continues in force as long as the premiums are paid. This type of insurance is mainly for protection but also has a moderate investment feature. Because a portion of the premiums are set aside to build up a cash value, the premiums are higher for each $1,000 of protection than for term insurance. It is the most inexpensive type providing permanent protection. More people buy ordinary life insurance than any other kind.

Limited Payment Life Insurance is a plan of insurance for the whole of life but the premiums are payable for a specified number of years only. Payments are usually for 10, 20, or 30 years, or to age 65, but the face value of the policy is not paid until death. In other respects, it is much the same as ordinary life. The premiums are higher, because they are paid for a limited time, and lim-

ited payment life, therefore, contains more of an investment feature than does straight life.

Endowment Insurance provides for premium payments for a specified number of years, after which the face value is payable to the insured. Protection is provided to the extent that if the insured dies at any time before the policy matures, his beneficiary receives the face value of the policy. Premiums are highest on this type of policy because it gives a minimum of protection and a maximum of investment for the money spent.

A comparison of the premium rates for the four basic types of policies clearly shows the difference in costs between those which stress protection—term and straight life, and those which stress investment—limited payment life and endowment. These are the annual premium rates listed for one company for $1,000 insurance taken at age 25:

10 Year Term.........$ 7.57
Straight Life $18.70
20 Payment Life.......$32.66
20 Year Endowment....$49.27

The basic types of policies are combined in many ways to create policies for special groups of buyers. One of the most popular of these combination policies is *Family Income Life Insurance*. It is designed to give maximum protection to the insured while his family is growing, with decreasing protection in later years. Here is an outline of this type of policy: If a man buys a $10,000 20-year family income policy, he will be insured for $10,000 for the rest of his life. He will also have extra protection during the first 20 years. If he bought his policy in 1957 and died a short time later, his family would get $100 a month until 1977. Then, in 1977, his family will get $10,000. If he dies after 1977, his family gets only the $10,000.

TABLE 3. A Comparison of Insurance Premiums by Type of Policy
Annual Premium Per Thousand Dollars Insurance

Age at issue	Type of policy			
	10 Year term	Ordinary life	20 Payment life	20 Year endowment
20	$ 7.27	$16.24	$30.42	$50.18
30	9.10	21.31	36.32	51.41
40	13.66	29.48	44.50	54.40
50	24.87	42.98	56.75	61.65
60	40.57	66.26	77.49	78.11

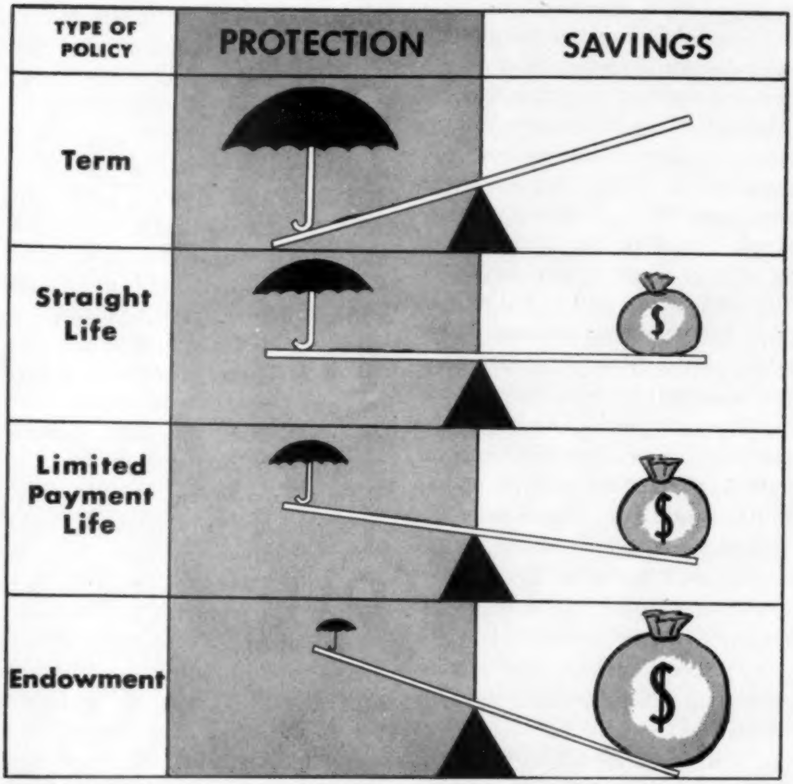
Source: Little Gem Life Chart, 1956, National Underwriter Company—average of policies offered by five selected companies.

TABLE 4. A COMPARISON OF PROTECTION AND SAVINGS FEATURES BY TYPE OF INSURANCE POLICY

Size of Policy $100 Annual Premium Will Buy at Age 25

Type of policy	Size of policy	Proportion of premium for		Cash value in 20 years
		Protection	Savings	
	Dollars			*Dollars*
20-year term	10,000	all	none	none
Straight life	5,000	1/2	1/2	1,300
20-payment life	3,000	1/3	2/3	1,650
20-year endowment	2,000	1/5	4/5	2,000

Amounts are approximate. Provisions of different companies vary.



Each dollar spent in premiums is divided like this when insurance is purchased at age 25.

Special Sources and Types of Life Insurance

Most life insurance policies held by farmers are one of the four major types described, or a combination of them. There are several other types and sources of life insurance of less importance to farmers.

Group Life Insurance is of growing importance in the economy. This is life insurance on a wholesale basis. Term insurance is offered to a group of employees under a company or institution plan. Medical evidence of insurability is seldom required. The cost is low because of savings through volume sales and low collection costs. In many group plans, the cost is the same regardless of age of the insured. This makes group insurance an especially good buy for older members of the group, but not so good for younger members. Many group plans allow the group member to convert his term insurance to a permanent plan if he leaves the company or institution. Unfortunately, few farmers have an opportunity to use group insurance.

Industrial Life Insurance is written in small units on a weekly or monthly premium basis, and premiums are often collected by a company representative. The cost of protection is high because the costs of writing the insurance and keeping it in force are high. This type of insurance is of less importance than formerly, but still represents about 10 per cent of all life insurance in force.

Credit Life Insurance is written through lending institutions on the lives of borrowers or installment purchasers. It guarantees full payment of the loan in case of death. This plan is growing rapidly and has recently been adopted by some farm loan agencies. As with group insurance, the cost is usually the same regardless of age of the borrower, making this insurance especially attractive to older borrowers.

Annuities are not a form of life insurance in the usual sense. Their purpose is to assure definite income for a period of time—usually for someone's life. With annuities, premiums are paid, either in lump sum or in installments, and in return the insurance company pays back a sum of money at stipulated intervals for a specified time. The payments are usually made for as long as one person or as long as either of two persons shall live. Life insurance policies usually have an annuity feature as an optional payment plan.

A great majority of the life insurance in force is written by legal reserve companies. However, veterans' life insurance, issued by the Federal Government, totaled over 40 billion in force in 1956. Minor sources of insurance are: fraternal life insurance, issued by societies, lodges and other such groups; savings bank life insurance, issued only in New York, Massachusetts, and Connecticut; life insurance issued

by assessment associations and mutual aid groups.

The Insurance Policy

An insurance policy is a written contract between the insured and the company. Most policyholders rightfully guard the policy as a valuable possession, but few take the time to read it, understand it, and use it. Every policyholder should know what his insurance policy is worth in cash, how much and under what conditions he can borrow on it, how dividends may be used, whether he can change the type of policy, what settlement options are available, and what his alternatives are if he can no longer pay the premiums. At first glance, the policy may appear to be a formidable document, but if the policyholder knows the important provisions to look for, it can be easily understood.

Cash Values—The policyholder can decide to surrender his policy at any time. The company then has no further obligation, and will refund to the policyholder the savings or reserves accumulated under the policy. The amount which will be returned at any time is the cash value and depends on the size and type of policy, length of time it has been in force, and the age of insured at issue. No savings are accumulated with Term Insurance, so that it has no cash value. A table of cash values is generally prominently displayed in other contracts, and it is a simple matter to read off the cash value at any time. This represents an investment somewhat comparable to a savings account in a bank. A person invariably knows how much money he has in his bank account, and should also know how much he has in his "life insurance account."

Loan Values—The table of cash values in the contract is also used to determine how much the insurance company will loan against the policy. The insured may borrow without giving up the policy and disrupting his life insurance program. Another alternative is to use the policy for collateral in borrowing from a bank or other source. Here, too, the cash value determines the value of the policy as security for a loan.

Non-Forfeiture Provisions—If the policyholder fails to pay his premium when it is due, he has *grace period* of one month during which the insurance remains in force and he can pay the premium without penalty. If he fails to pay within the period of grace, he has defaulted in his contract and the insurance protection ceases. However, his savings or investment in the contract is protected by the non-forfeiture provisions. These usually provide three alternatives: He may take his savings in cash; he may take a paid up policy for such part of the original amount as the savings will buy; he may take paid up, extended term insurance for the same amount as

the original policy and for as long a term as the savings will buy. The amount of paid up life insurance or the length of extended term insurance which would be forthcoming at any time can easily be determined by reading the tables in the policy.

In addition to the above choices when defaulting on a contract, the insured usually has the option of *reinstating* within a specified period by passing a medical examination and paying overdue premiums with interest. The policy may also contain the *automatic premium loan,* under which the company borrows against the cash value of the policy to pay the premiums as long as the cash value lasts unless instructed to do otherwise by the insured.

Before allowing a policy to expire, the insured should know what his alternatives are under the terms of the contract and select the option that will make best use of the dollars he has "banked" with the insurance company. He should also realize that it seldom, if ever, pays to let one policy expire and take out another.

Dividends—Like any other business, an insurance company must match its income against its expenses. Because death rates and operating expenses cannot be predicted with 100 per cent accuracy, the company must have an operating margin to work on, and set premium rates accordingly. The margin creates a surplus, and at least part of this surplus is distributed to policyholders as dividends. Some companies offer non-participating policies which do not share in this division of surplus, but most policies are participating policies and do receive dividends. However, the amount of the annual dividend varies with the experience of the company. It is common to return higher dividends on policies with a high investment feature than on policies with a low investment feature. The net cost of the insurance is the premium *minus* the dividend. The net cost is more important than premium when comparing the cost of insuring in various companies.

The policyholder has important options in the use of dividends. In general, he can: (1) take the divi-

dend in cash or use it to reduce the annual premium; (2) use it as a single premium to purchase paid up insurance; (3) leave it with the company to accumulate interest, to be withdrawn at the will of the policyholder. The best option depends on circumstances. For example, if the insured's current need is for cash, he should take his dividend in cash or use it to reduce the annual premium. If he can't pass a medical examination and needs more insurance, he should take paid up insurance. If he wants a conservative investment, he should "bank" the dividends with the company.

Privilege to Convert—An important provision in most insurance contracts gives the policyholder the right to exchange the policy *without medical examination* for a new policy of the same face value but of a higher investment type. In other words, the option to exchange an Ordinary Life policy for a Limited Payment Life or Endowment policy, but not for a Term policy. With the exchange, the insured may make up the difference in premiums since issuance of the policy, plus interest, and receive premium rates under the new policy based on age at time of original issuance. It is often possible to make the exchange without making up difference in premiums since issuance by taking a policy of lesser amount. An additional alternative often offered is to convert at the attained age of the insured, so that no back premiums or interest need be paid.

This feature is useful in revising an insurance program to fit changing family circumstances. As years pass and the family grows, the need for protection may become less or remain stable while cash demands become less critical, making it possible to introduce more investment features into the insurance program.

Double Indemnity and Disability Waiver of Premium—With most policies it is possible to add either or both of these features for a small additional expense. The amount of

TABLE 5. Double Indemnity and Disability Waiver of Premium Rates
One Major Company, Ordinary Life Policy

Age at issue	Annual basic premium	Additional premium for: Waiver of premium	Additional premium for: Double indemnity
15	$13.79	$ .90	$ .34
25	17.59	.94	.47
35	23.59	1.04	.80
45	33.64	1.18	1.54
55	50.46	1.46	4.14

Source: Little Gem Life Chart, 1956, National Underwriter Company.

additional cost varies with the type of policy, age at issuance, and the company. Rates for one major company offering these features are illustrated in table 5. Only rates on this company's ordinary life policy are shown.

The disability clause provides for waiver of premium in case the insured becomes totally and permanently disabled while the policy is in force. Even though the chance of total disability is slight, the totally disabled policyholder would still need protection for his dependents and would often find it impossible to continue to pay premiums. For this reason, it seems advisable to pay the small additional premium and have the waiver of premium clause.

A few companies offer *disability payments* in addition to waiver of premium in case of disability. The additional premium on such contracts is based on the amount of the disability payment and the length of time it will be paid. This provision amounts to combining health insurance with life insurance. It is usually more logical to provide for health and accident insurance needs in separate policies.

Double indemnity provides for doubling payments to the beneficiary in case of accidental death of the insured. The contract generally specifies that death must occur within 90 days of accident if double indemnity is to apply. There is little logic, from a dollar and cents viewpoint, in this provision. The beneficiary's *needs* are not doubled if the insured meets death accidentally. While the extra premiums are slight, the chance of accidental death is also much less than most people realize. Table 6 shows the distribution of deaths by cause in 1956 among all holders of ordinary life insurance. If the deaths due to motor vehicles are added to other accidents and homicides, they total less than 7 per cent of all deaths. Further, some deaths classified here as accidental would be excluded from double indemnity benefits because of limitations on the definition of accidental death in the insurance contract. Deaths resulting from war, and from gas or poison, for instance, are excluded.

Settlement Options—Life insurance policies provide that at death of the insured a *cash settlement* will be made for the face value of the policy. As alternatives to a cash settlement, several methods of payment are offered. The insured may select an option and thus specify how the proceeds are to be paid to the beneficiary at his death. If the insured does not so specify, then the beneficiary may elect the option at death of the insured.

Many variations of settlement options are written into insurance contracts. In New York State the law requires that four specific options be offered in all life contracts. These four options, with some common variations are as follows:

TABLE 6. Distribution of Deaths by Cause
Ordinary Insurance Policyholders, 1956

Cause of death		Per cent of deaths
Cardiovascular-Renal Diseases:		
Cerebral hemorrhage	9.4	
Diseases of the heart	43.3	
Nephritis	1.1	
Other	3.4	
Total		57.2
Cancer		18.6
Pneumonia and influenza		2.2
Tuberculosis (all forms)		.5
Diabetes		.9
Pregnancy and childbirth		.1
External Causes:		
Motor vehicle accidents	3.1	
Other accidents	3.1	
Suicides	1.9	
Homicides	.2	
Total		8.3
All other causes		12.2
Total all causes		100.0

Source: Life Insurance Fact Book, 1957, Institute of Life Insurance.

1. *Equal installments of a given amount.* The beneficiary elects the amount of income desired monthly. This amount is paid until all proceeds of the policy are returned to the beneficiary. Of course, the length of time the payments will continue depends on the size of the policy and the size of monthly income elected by the beneficiary.
2. *Equal installments for a specified length of time.* The beneficiary decides how long income from the policy is needed. The calculation is then made as to the amount which can be paid each month from the proceeds of the policy.
3. *Life income option.* The basic provision in this option is for equal installments as long as the beneficiary shall live. The size of each monthly installment will depend on the age and sex of the beneficiary at death of the insured, as well as the size of the policy. Three variations of this option are the *no refund option,* the *certainty option,* and the *installment refund* option. If the *no refund option* applies, payments cease at death of the beneficiary, regardless of how soon after payments start this death occurs. If the *certainty option* applies, payments are guaranteed for a specified period (usually 10 or 20 years) and as long thereafter as the beneficiary lives. If the *installment refund* option applies, the payments are guaranteed for the life of the beneficiary, but in the event the beneficiary dies before the proceeds of the policy have been paid in full, the payments will continue until they are paid in full. If the *no refund option* is selected, the payments will be larger than with the *certainty* or the *installment refund* option.
4. *Interest option.* The proceeds of the policy are left with the company and the company pays interest at not less than rates specified in the policy.

The cash settlement is useful to provide funds for expenses of death and the payment of debts. However, the greatest need for insurance proceeds is usually to provide steady income over a period of time. Whether this period of time is measured in years or in the life of the beneficiary depends on family circumstances. Selection of settlement options is an important part of estate planning. Whether the settlement option should be selected by the insured or left to the discretion of the beneficiary depends on family circumstances.

Commonly, some insurance would be needed for cash, some for income over a period of years. It is important to study the settlement options of each policy with care before deciding which ones are to be used for cash and which ones for income over a period of time.

It is senseless to pay hard earned

dollars for insurance protection over many years without spending some time in the careful planning for the use of that protection at death. A well trained insurance agent can lend valuable assistance in planning for the use of insurance dollars.

Life Insurance Carried by New York Farmers

A study of the insurance practices of 587 farmers in New York State has shown that more than three-fourths of the farmers contacted had provided a life insurance program of some type to insure their own lives. About a third of the operators had insured themselves but no other member of the family. In almost half of the cases, however, the operator had decided to provide an insurance program for one or more other members of his family. The amount carried on the operator averaged $6,219 and was most frequently a Limited Payment type policy (table 7).

TABLE 7. Type and Average Size of Life Insurance Policies on **587 Commercial Farms, New York, 1953**

Type of policy	Per cent of policies	Average size	Per cent of total amount of insurance
Ordinary Life	27	$2,652	32
Limited Payment	38	1,772	30
Endowment	31	2,159	30
Term	1	6,224	4
Family Income	1	4,295	2
Other	2	2,181	2
Total or average	100	$2,222	100

Ordinary Life insurance, though not the most frequent type of insurance purchased by this group, accounted for the greatest share of the total amount of insurance carried by these farmers.

Life insurance premiums accounted for 35 per cent of the total dollars spent on insurance on these farms. Those farmers with insurance paid out an average of $239 annually for their life insurance. The majority of this cost was for insurance on the farm operator.

How Much and What Kind of Insurance to Buy

The two most important questions any buyer of insurance faces are: how much insurance and what kind should I buy?

There is no rule of thumb which can be used to determine how much insurance a person should carry, or what kind he should carry. The problem of each individual is to determine what his insurance needs are, how much he can spend for insurance, and then to spend it in a way that will best cover his needs. More than dollar and cents calculations go to determine the "need" for, and the amount which "should be" spent for insurance. The relative importance placed on "living it up" today as opposed to "saving for a rainy day" by the family is a determining factor.

The typical farm owner would like to make provisions so that if he died tomorrow, his family could continue to enjoy the same standard of living as if he had lived a normal life. However, few people can carry enough insurance to make such provisions.

Farm income goes first to keep the family fed, clothed, and sheltered. Farm operating expenses get the next call; the taxes have to be paid, feed bought, the hired man paid and so forth. After family living and farm operating expenses are taken care of, there is something left for debt payments, life insurance, and other things. It has been strongly argued that it is fully as important to "plan for tomorrow" with life insurance as to eat and pay the bills today. In practice, however, immediate problems get first attention, and those which can be will be postponed. The result is that the amount of cash a farm family can and will set aside seldom, if ever, buys all the life insurance the family would like to have. That's why it's very important to examine carefully the various needs of life insurance and to spend the available money on the most pressing needs.

A Farmer's Needs for Life Insurance

Farmers find many uses for life insurance. There are many financial needs to be met at the death of a farm operator. An insurance program should consider all of the needs that might arise, and in buying insurance, it should be recognized that some of these needs have priority over others.

Family income. Income to the family in case of death of the breadwinner is by far the most important reason for carrying insurance. To best cover this need with a given amount of money to spend on insurance, policies which feature protection are needed. The need for protection is greatest while the family is young, and decreases gradually over the years.

Life insurance is especially valuable for family protection because it is paid immediately and directly to the beneficiary and does not go into the general estate of the insured. Furthermore, the proceeds of a life insur-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ance contract cannot be attached for the debts of the insured.

Debt Insurance. Insurance to cover indebtedness of the business is really the same as providing income to the family, because if a farmer dies and leaves the business free and clear, or enough insurance to cover indebtedness, the family has the farm capital to live on. This also calls for insurance that features protection.

A cash fund to cover expenses of death. There are always expenses associated with a death in the family. It may be important to see that some funds are available in cash for this purpose.

Income in later years. Savings can be accumulated in the form of high investment type life insurance to provide retirement income. Most farmers prefer to provide for retirement by building up a successful farm business so that they can retire on the income from the operation or sale of the business. Social Security is also available for this purpose.

Insurance as an investment. A good farmer can realize a better return on money invested in his farm business than on money invested in high savings insurance, such as limited payment or endowment. A farmer who is bor-

rowing money to operate his business and at the same time paying premiums on insurance policies which feature investment is paying higher interest rates than he is receiving. A wiser course to follow would be to spend his insurance dollars primarily for protection and use his farm for investment. A farmer who has his farm paid for and has little need for greater investment in his business can add diversity and stability to his financial program by investing in life insurance or other conservative investments.

Saving for a college education. It

certainly is good business to plan for the education of the children. However, this represents a need for saving rather than insurance on the children. There are many ways to save for the education of the children. Investing in insurance is one way. If this method of saving is chosen, the insurance should be carried on the life of the breadwinner, so that whether he lives or dies, funds will be available for the children's education. As a child's death would seldom cause loss of income to the family, there is little need for protection in this form.

Insurance on the farmer's wife. A farm wife contributes much to the farm business in addition to all the usual functions she performs as wife and mother. The death of a farm wife commonly does create a heavy economic burden. It is logical to use insurance as protection against this loss. However, this need for insurance should be rated less important than insurance on the life of the breadwinner.

Building an Insurance Program to Fit the Farm and the Family

In looking over the needs which a farmer has for life insurance, it becomes evident that the protection feature is generally more important to a farmer than the investment feature.

The recent survey of insurance programs of New York farmers showed that about 60 per cent of their life insurance was in investment type policies—limited payment or endowment. This is a definite indication that farmers are underemphasizing the protection feature of life insurance.

A young man struggling to provide for a growing family and pay for a farm has a particular need for insurance. If he lives and stays healthy, he will eventually pay for the farm. When the farm is paid for, he and his family will have income from his labor and from the capital invested in the farm. If he dies after the farm is paid for, his family will have the income from sale or operation of the farm. Few families owning a good farm free and clear would suffer from want. The real risk the family takes is that the young man will die before the debts are paid.

A young man who is in debt for his farm and has a growing family thus has an urgent need for life insurance protection. He seldom, if ever, is in a position to use life insurance as an investment.

Determining Protection Needed

The amount of protection the family needs depends to a degree on what the family expects as a level of living. The amount of property in the form of insurance,

a farm, Social Security, and so forth, which is needed to provide a given level of income over time can be estimated.

Assume a farmer named Joe Hill has a wife, age 40, and two children, ages 12 and 6. Assume further that the Hill family has estimated that the monthly income requirements in the years ahead, if Joe were to die immediately, are as follows:

$250 per month for 12 years—when the youngest child will be 18

$150 per month for the next 13 years—this brings the widow to age 65

$100 per month for the remainder of her life

These monthly requirements, which seem fairly conservative, would require a fund of approximately $55,000 (with interest at three per cent). This does not provide for expenses of college training for the children. Neither does it provide for a major illness or accident.

The size of the fund needed to fit other programs could be estimated from table 8. It is obvious that even rather conservative programs require a sizeable amount of money.

TABLE 8. Amount of Money Needed to Provide Monthly Income of $25
Interest at Three Per Cent

Years income will be needed	Amount required	Years income will be needed	Amount required
1	$ 296	7	$1899
2	583	8	2140
3	862	9	2374
4	1133	10	2600
5	1396	15	3639
6	1651	20	4535

Source: Little Gem Life Chart, 1956, National Underwriter Company.

Determining Resources Available

Once the size of the fund needed to care for dependents is determined, the next step is to turn to the resources available to meet this demand. It is probable that there will be several sources which may be used to meet the needs of the dependents. All should be considered. These will strongly influence the amount of life insurance needed.

At least some of the assets of the farm business will surely become available. The way the farm property is held by the farmer at death and the method of disposition of these assets after death, however, will have important bearing on the


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amount of assets available to the members of the family. If there is no will or other plan for disposition of the estate, the laws of New York and most other states provide for a sharing of the estate by the heirs. If the children are all minors this will create certain immediate problems, for the laws are designed to give every possible protection to minors in estate settlements. If the children are adult, they may wish to claim their share of the assets immediately. *One of the best and cheapest "life insurance" policies a farm owner can leave for his family is an up-to-date will.*

If the farm is not broken up by the provisions of the will or intestate settlement, there still will be the problem of whether to sell the farm or try to operate with a manager or hired labor. The farm owner and his family should have an understanding as to what should be done with the farm in the event of his death.

Consideration should also be given to the fact that most farmers are now eligible for benefits under Social Security. Survivor's benefits can be considerable and must be carefully weighed when building an insurance program. Table 9 presents survivor's benefits that might be forthcoming to a farm family.

Benefit payments are made for unmarried children under 18, for widows with such children, and for widows 62 or over. No benefits are paid to widows under 62 without dependent children.

To illustrate the effect of these benefits on the insurance program, consider again the example of the Hill family. Joe Hill dies leaving his widow, age 40, and two children ages 12 and 6. If Joe's reported earnings under self-employment averaged $200 per month, the beneficiaries would receive the following monthly benefits: $157 for six years, when the oldest child reaches 18; $118 for the next six years, at which

TABLE 9. Survivor Benefits under Social Security

Average net annual earnings	Monthly payments		
	Widow or child	Widow and one child	Widow and two children
$ 540	$30.00	$ 45.00	$ 50.20
1,200	41.30	82.60	82.60
1,800	51.40	102.80	120.00
2,400	58.90	117.80	157.10
3,000	66.40	132.80	177.20
3,600	73.90	147.80	197.10
4,200	81.40	162.80	200.00

Source: "Your Social Security," U. S. Department of Health, Education and Welfare, Social Security Administration, OASI-35, p. 13, October 1954.

time the youngest child is 18; nothing until the wife reaches 62; and then $59 for the remainder of her life. The amount of insurance that would be required to support a similar program would be approximately $23,000. The above illustration assumes full benefits in that outside earnings of the widow are not to exceed $1,200 annually. Even with these qualifications, however, it is evident that Social Security can go far in meeting the needs of dependents and will change the need for insurance.

Another consideration in calculating what the dependents will need is their training or ability to earn income. If the wife is trained as a teacher, for example, this fact may diminish the size of the fund or protection that is necessary in case of death of the farm operator. However, a widow with small children is in a poor position to take over the job of family breadwinner.

Still another factor to be considered in determining family needs is the likely change in pattern of living. If the family is accustomed to farm living, and the logical step would be to sell the farm at death of the breadwinner, the need for cash income after moving from the farm is likely to be underestimated. Non-cash farm income for the average farm family is a significant item.

In weighing the effect of the death of the farm operator, it is logical to examine the financial *needs* of the dependents and then to see *what resources* are available to meet these needs. In a great majority of families, life insurance is needed to meet the difference between needs and resources. In terms of the Hill family, Joe needed a fund of approximately $55,000 to meet the future demands of the dependents plus an estimated $5,000 for a clean-up fund. To meet this fund of $60,000, he would have at least the clear assets of the farm plus any additional benefits such as Social Security, etc. To carry the example further, assume that Joe has a net worth of $25,000, Social Security survivor's benefits equal to $23,000, but no other sources of support for his dependents. In this situation, it follows that Joe Hill could meet the desired program with $12,000 worth of life insurance.

Balancing Needed Protection Against Dollars Available for Insurance

The following examples illustrate further how farm families in different circumstances might decide how much and what kind of insurance to buy:

Bill Jackson is 25 years old. He has a wife 24, a son 3, and a daughter 1. He has been farming two years and is heavily in debt. He has no life insurance but has been an employee or self-employed under Social Security for six years. The average earnings reported for Social Security have been $1,800 a year.

Thus, if he were to die now, his wife and children would have $120 per month until the son reached 18, then $103 per month until the daughter reached 18. Thereafter no Social Security benefits would be payable to his widow until she reached 62. She would then receive $51 per month for life unless she remarried (see table 9). He believes that if he were to die now, his wife could sell the business, pay all debts, and have $5,000 left. He knows $5,000 and Social Security benefits wouldn't take care of his wife and children, and wants to buy as much protection for them with life insurance as possible. He thinks that he can put about $100 a year into life insurance.

For insurance purchased at age 25, $100 a year will pay the premiums on:

a $2,000—
  Twenty-year endowment policy
or a $3,000—
  Twenty payment life policy
or a $5,000—
  Ordinary life policy
or a $12,000
  Ten-year term policy

Bill Jackson needs all the protection for his family that he can get. He decides to buy term insurance, and hopes to convert it to ordinary life in a few years. He also hopes to be able to buy more life insurance as soon as he is better established in his business.

Henry Sands is 40 years old. He has a wife 38, a daughter 14, and a son 11. He has been farming 12 years and has built up a good equity in his business. He believes that if he were to die now, his wife could sell the business, pay all debts, and have $20,000 left.

He has been paying Social Security taxes as a self-employed farmer since 1955, and has paid the tax on $2,400 of net farm profit each year, or $200 of monthly earnings. Thus his family's Social Security benefits would be $157 per month until his daughter reached 18, then $118 per month until his son was 18. After that, his widow would receive no Social Security benefits until age 62, when she would receive $57 per month for life. Her remarriage would cancel benefit payments to her.

He knows that Social Security and the $20,000 fund would provide a small income for his wife for her lifetime, but he wants his insurance to provide more protection for her. He has a $5,000 ordinary life policy which he took out at age 25. The premiums are $100 annually. He thinks that he can now spend a total of $250 annually for insurance premiums. The next ten years —until his son reaches age 21—is the period when the family needs greatest protection. Henry Sands sensibly decides to continue his $5,000 ordinary life policy and to spend the extra $150 annually for a policy or policies combining term and ordinary life in a way that will give greatest protection for the next

ten years. He might find a family income policy suited to his needs.

Both Bill Jackson and Henry Sands made their decisions on life insurance in the following way:

They decided how much protection their present resources would provide.

They decided how much protection their families needed.

They decided how much they could spend on insurance.

They decided what types of policies would come the closest to meeting the family needs with the money they had to spend.

Partnership Insurance for the Farm Business

Partnership purchase and sale agreements financed with life insurance are quite common in the business world. They are much less commonly found between farm partners. In some cases, however, they have worked extremely well as a method of transferring farm ownership to the next generation. It is possible that such agreements can perform a useful service over a wide range of transfer situations.

In general, the plan consists of two parts: (1) a written agreement between business partners in which each binds himself and his estate to sell his interest in the enterprise to the surviving partner, or partners, at a stipulated price and, at the same time, binds himself to buy in the event of his partner's death; and (2) life insurance policies carried by each partner on the other, the proceeds of which are to be used to carry out the purchase and sale agreement.

The subject of business insurance is very large and technical. The validity of well-drawn agreements of this nature has been established by the courts. It is imperative that a lawyer's help be obtained in preparing the contracts.

Chief obstacles to use of partnership insurance in the farm business are the wide difference in ages of the partners, the disproportionate share in ownership, and the late start fathers and sons commonly get in initiating the partnership. The inability to carry insurance on each partner up to the full amount of his equity in the business should not eliminate the possibility of some coverage by insurance. Too little attention is given to partial coverage plans. *It is imperative that farm partners have a definite written agreement for the disposition of jointly owned property at death of a partner.* It is not necessary that this agreement be financed with life insurance, but its use for this purpose does have advantages as well as disadvantages. The most common advantages listed for its use are:

1. The survivors' security of future ownership is assured. Usually, of course, the survivor will be the son.
2. The estate of the deceased partner can be promptly settled.

3. All heirs can obtain their equity from the business in a predetermined and fair manner.

The disadvantages that seem most important are:

1. Premium payments represent a severe drain on the business. In fact, sufficient cash may not be available to carry insurance in significant amounts.
2. The money invested in insurance cannot be expected to earn as large a return as if it were invested in the farm business.
3. One or more partners may prove uninsurable.

A farmer in partnership should develop an insurance program which, first of all, provides income protection for his family. Partnership insurance seldom provides a major function towards that end.

Advice to Life Insurance Buyers

A life insurance program must be tailored to fit the needs of the individual. There are a number of general principles to keep in mind when building an insurance program:

1. The family breadwinner should be covered first to protect the family from loss of income. Insurance on the other members of the family is of much less importance.
2. A farmer or any other owner of a business needs a different kind of insurance program than does a salaried man or a man working for wages. As a businessman, the farmer should build his insurance program in a businesslike way.
3. A farmer's business usually offers a better opportunity for investment than does life insurance. Therefore, a majority of farmers need protection more than investment.
4. A farmer's needs for life insurance are greatest when his family is young. He should change his insurance coverage to meet his changing needs.
5. It's important for a farmer to start his insurance program while young because a young man usually needs insurance more than an older man. Family income policies are especially well adapted to the needs of many young farmers.
6. It's poor business to allow insurance policies to lapse or to cash in a policy in order to buy another kind. Select policies with the intention of keeping them in force.
7. There is no one best type of policy. Don't think you have to fill all your insurance needs with one policy. You can build a program better fitted to your needs by taking a number of small policies which added together give you the protection you want. Several small policies can distribute the premiums throughout the year.

8. Settlement options are important. The proceeds of a life insurance policy can be paid to the beneficiary in almost any way the policyholder may wish. Here are things to keep in mind in selecting settlement options:
   a. The widow will need some money to clean up debts and pay death expenses.
   b. The dependent's greatest need will be for a continuing income.
   c. The widow will need income most while the children are growing.
   d. Allow some flexibility—you can't foresee family changes or changes in economic conditions which will affect the needs of dependents.

9. Insurance should be a family program. See to it that your family knows what insurance you have and what it is supposed to do. Keep your policies where they will be readily accessible to your family in case of your death. You may want to keep a list of your insurance policies, with policy numbers, in a safe deposit box.

10. Let your insurance agent work for you. It's true that he is selling insurance. It's also true that it is to his benefit to help you understand what your insurance program can do for you. A good agent is prepared to do this. Make use of his knowledge.

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